

Press Release

MegaFon Announces Audited Financial Results for the Year 2011

March 1st, 2012, MOSCOW, Russia - Open Joint Stock Company “MegaFon”, a Russian universal telecommunications operator, announces its consolidated financial results¹ for the fourth quarter and twelve months ended December 31, 2011.

Key Consolidated Financial and Operational Results for the year 2011:

In 2011, MegaFon achieved impressive financial results and demonstrated strong revenue growth in all business areas.

- Consolidated revenue grew by 12.6% year-on-year (y-o-y), to RUR 242,608 million.
- OIBDA increased by 3.1% y-o-y, to RUR 100,822 million, a record-high level in the Company’s history.
- OIBDA margin was 41.6% versus 45.4% last year.
- Net Income decreased by 11.4% y-o-y, to RUR 43,579 million.
- Free Cash Flow reached RUR 24,412 million.
- Net Positive Cash Position as of December 31, 2011 was RUR 45,689 million.
- The number of active mobile subscribers as of the end of 2011 was 62.8² million, an increase of 9.6% y-o-y.

¹ US GAAP

² Consolidated data includes subscribers of the Company in Russia and subscribers of its subsidiaries: TT-mobile CJSC in the Republic of Tajikistan, Aquafon GSM CJSC in the Republic of Abkhazia and Ostelecom CJSC in the Republic of South Ossetia

Key Consolidated Financial Results for Q4 2011

- In Q4 2011, consolidated revenue grew by 11.0% y-o-y, to RUR 65,462 million.
- OIBDA decreased by 3.4% y-o-y, to RUR 25,232 million.
- OIBDA margin declined to 38.5% versus 44.3% in Q4 2010.
- Net Income decreased by 23.6% y-o-y, to RUR 9,670 million.

MegaFon continues to develop in accordance with its previously announced strategy and to demonstrate strong growth. The numbers reflected in our current financials are in line with our expectations and are driven by the implementation of strategic initiatives that are aimed at providing a wider spectrum of services and at enhancing customer experience. One part of this strategy is adding coverage and service through acquisitions -- and, in line with this, the Company made a number of acquisitions in 2011: the NetByNet Holding group and Web Plus in June 2011, Nakhodka Telecom and ChebNet group in November 2011, and Luchshe.Net and Ugratel in December 2011.

Sergey Soldatenkov, Chief Executive Officer of MegaFon, commented on the financial and operational results as follows:

“We are quite satisfied with the Company’s financial performance in Q4 2011 and the full year of 2011, and are gratified that our balance sheet remains the strongest in the industry. We continued to invest actively in network development, in acquiring new assets and in developing our own retail chain. There is no doubt that our investment programme, which is the largest in our industry, our active M&A policy and our strategic marketing initiatives have all impacted our net income due to higher depreciation and amortization charges and other expenses related to our investments in our business. But we were ready to absorb those charges in the short run in order to build a stronger competitive advantage for the Company in technology and improved service for our customers in the long run. And our net income remains among the highest in the industry.”

Capital investments in Russia in 2011 amounted to RUR 68,701 million, an increase of 5.0% y-o-y.

Mobile Internet continues to be a key driver of revenue growth for the Company. For the full year 2011, Russian mobile data revenue grew 50.0% y-o-y, to RUR 29,947 million. In the fourth quarter of 2011, mobile Internet revenue increased by 41.6% and 16.7% against the fourth quarter of 2010 and the third quarter of 2011, respectively.

Full year Russian wireless revenue in 2011 grew by 9.3% y-o-y, to RUR 225,422 million, reflecting continued subscriber base growth. In the fourth quarter of 2011, wireless revenue grew 9.1% y-o-y. The quarter-on-quarter wireless revenue growth of 2.1% was due to seasonality.

The VAS share of Russian wireless revenue for the full year 2011 reached 25.2% versus 21.8% in 2010.

“In December 2011, we adopted record low international roaming tariffs for all the Company’s customers in 44 countries in Europe, including the European part of CIS and Turkey. Now our customers need not be concerned about activation or deactivation of tariff options, buying tourist SIM-cards, and other schemes to avoid roaming charges which also had the effect of radically limiting access to communications while travelling in Europe. Unlike tariffs offered by our competitors, our base tariff is also activated automatically for the most active users of our roaming services, our corporate customers, which means that both private and government companies can also save significant amounts of money. Our key principles are minimum prices, maximum convenience and easy roaming for customers. I am pleased to note that, following the adoption of our new policy, growth in roaming services usage turned out to be significantly higher than expected, while the decrease in revenue in this business area was less than forecast,” said Sergey Soldatenkov.

Investments in technology development and expansion of our own retail network allowed MegaFon to expand its subscriber base to 61.6 million customers in Russia. Net additions in subscribers over 2011 were over 5 million.

“It is very important to note that in 2011 MegaFon was not striving for leadership in gross adds. We avoided the so-called “subscribers chase at any cost”, and instead focused on improving the quality of our subscriber base by closely monitoring new additions and continuing to develop our own retail chain as a means to achieve this. Our long-term strategy is to provide ever-improving customer care, to offer the most interesting services and goods, and to always be honest and open with our customers. Customer confidence and the provision of the best service form the basis of MegaFon’s leadership in the Russian market,” said Sergey Soldatenkov, in conclusion.

Key corporate events of the year 2011:

- In June 2011, MegaFon acquired 100% of the shares of the NetByNet Holding group, a further important step in our strategy to become a universal telecommunications operator, by further strengthening our fixed-line portfolio. The acquisition of NetByNet allowed MegaFon to enter the fixed broadband Internet access, digital TV and IP-telephony markets of Moscow, Moscow Region, Belgorod, Voronezh, Lipetsk and Orel Regions.
- In July 2011, MegaFon undertook re-branding of its subsidiary in Tajikistan. Now this company operates under the brand of “MegaFon-Tajikistan”. As of year-end 2011, the subscriber base of the branch exceeded 1 million.
- In October 2011, the Big Three Operators, Mobile TeleSystems, VimpelCom and MegaFon, successfully completed a joint project to construct a 2165-km backbone for providing mobile communications along the Amur motorway between Chita and Khabarovsk.

- In November 2011, MegaFon signed a partnership agreement with Scartel to jointly develop 4G LTE (Long Term Evolution) networks in Russia. As a result, the Company will be in a position to provide 4G LTE services in selected markets using Scartel equipment. In its turn, Scartel will be able to use the MegaFon's network infrastructure.
- In the fourth quarter of 2011, MegaFon made a number of acquisitions of regional fixed assets, further strengthening the Company's position in the regional fixed line communications and broadband Internet access markets. In particular, in November 2011 the Company acquired full ownership of ChebNet group, and also of Luchtse.Net, a broadband operator in Kursk, in December 2011. Also, in November 2011, the Company bought 100 percent of Nakhodka Telecom, which operates in the Primorski Territory; and in December 2011, the Company acquired Ugratel, one of the largest telecom assets in the Khanty-Mansisk Autonomous Region.
- In December 2011, the credit rating agency Moody's upgraded MegaFon's international corporate rating to the level of Baa3 stable outlook from the prior level of Ba1 stable outlook. With this credit upgrade, the Company achieves full investment grade status, and the highest credit rating ever achieved by any Russian telecommunications company.
- In 2011, MegaFon became the General Partner of the Russian national sledge-hockey team. On June 27, 2011, the Company signed an agreement with the Federation of Physical Culture and Sports of Physically Challenged People to allocate RUR 73 million to train the Russian sledge-hockey team for the Paralympic Games in 2014 in Sochi. MegaFon became the first private company in Russia providing such significant sponsorship funds to support a national paralympic team.
- At the end of 2011, a new organization within the Company named MegaLabs was established to develop innovative plans for, and to facilitate the expeditious launch of value added services. The establishment of MegaLabs is intended to help MegaFon reach leadership positions in markets associated with its core businesses (e.g., content and media, mobile finance, mobile advertising, cloud solutions, e-government, m-health, etc.). The new company is focused on fast delivery of advanced products and services to the market, and, to achieve this, will partner both with well-known market participants and young designer teams. MegaLabs will also serve as a platform for MegaFon's other experimental developments.

Key Consolidated Financial Data (In millions of Rubles)³

	Three Months					Year		
	Q4 2011	Q4 2010	Q4 2011/ Q4 2010	Q3 2011	Q4 2011/ Q3 2011	2011	2010	2011/ 2010
Revenue	65,462	58,991	11.0%	63,433	3.2%	242,608	215,515	12.6%
OIBDA	25,232	26,108	(3.4%)	26,547	(5.0%)	100,822	97,774	3.1%
OIBDA Margin	38.5%	44.3%	(5.8 p.p.)	41.9%	(3.4 p.p.)	41.6%	45.4%	(3.8 p.p.)
Net Income	9,670	12,660	(23.6%)	12,475	(22.5%)	43,579	49,172	(11.4%)

Key Financial Data in Russia (In millions of Rubles)⁴

	Three Months					Year		
	Q4 2011	Q4 2010	Q4 2011/ Q4 2010	Q3 2011	Q4 2011/ Q3 2011	2011	2010	2011/ 2010
Revenue	64,930	58,524	10.9%	62,933	3.2%	240,742	213,956	12.5%
Wireless Business	60,160	55,129	9.1%	58,907	2.1%	225,422	206,306	9.3%
<i>Including data revenue</i>	<i>8,823</i>	<i>6,230</i>	<i>41.6%</i>	<i>7,559</i>	<i>16.7%</i>	<i>29,947</i>	<i>19,966</i>	<i>50.0%</i>
Wireline Business	4,770	3,395	40.5%	4,026	18.5%	15,320	7,650	100.3%
OIBDA	24,975	25,837	(3.3%)	26,198	(4.7%)	99,745	96,898	2.9%
OIBDA Margin	38.5%	44.1%	(5.6 p.p.)	41.6%	(3.1 p.p.)	41.4%	45.3%	(3.9 p.p.)
Net Income	9,591	12,610	(23.9%)	12,650	(24.2%)	43,853	48,918	(10.4%)
Net Income Margin	14.8%	21.5%	(6.7 p.p.)	20.1%	(5.3 p.p.)	18.2%	22.9%	(4.7 p.p.)
CAPEX	24,383	31,455	(22.5%)	15,728	55.0%	68,701	65,400	5.0%
CAPEX / Revenue	37.6%	53.7%	(16.1p.p.)	25.0%	12.6 p.p.	28.5%	30.6%	(2.1 p.p.)

In 2011, MegaFon continued its expansion in the fixed and broadband market of Russia which resulted in a growth of all wireline business statistics over prior periods.

Full year 2011 Russian OIBDA grew 2.9% y-o-y and aggregated RUR 99,745 million.

In the fourth quarter of 2011, OIBDA amounted to RUR 24,975 million, a decline of 3.3% versus the comparable quarter of 2010, which can be explained by a disproportionately higher growth of operational expenses relative to gross profit growth.

³ The Company consolidates financial results of Synterra Group since June 2010, Metrocom CJSC – since November 2010, NetByNet Holding group and WebPlus CJSC - since June 2011, Nakhodka Telecom LLC – since November 2011, Luchtse.Net LLC and ChebNet group – since December 2011.

⁴ Including mutual settlements with TT-mobile CJSC, Aquafon-GSM CJSC and Ostelecom CJSC

The quarter-on-quarter decline in OIBDA of 4.7% versus the third quarter of 2011 was due largely to the growth in operating expense resulting from one-off indirect expenditures related to the acquisition of new companies.

OIBDA margin for the full year 2011 amounted to 41.4%, a decrease by 3.9 p.p. y-o-y. Fourth quarter OIBDA margin fell to the level of 38.5%. The principal reasons for the decreases were the decreasing gross margin and growing ratio of OPEX to revenue due to the Company's increasing exposure to the lower margin businesses of fixed-line communications and mobile retailing.

Net income in Russia for 2011 decreased 10.4% y-o-y to RUR 43,853 million, which corresponds to a net income margin of 18.2% and today is the highest among the Russian peers.

In the fourth quarter of 2011, Russian net income reached RUR 9,591 million. The main reason for the decline in net income both on an annual and a quarterly basis is the growth of depreciation and amortization charges, which is the result of the Company's continuing significant level of investments in network construction in 2010 and 2011.

Key Operational Highlights of the Wireless Business in Russia

	Three Months					Year		
	Q4 2011	Q4 2010	Q4 2011/ Q4 2010	Q3 2011	Q4 2011/ Q3 2011	2011	2010	2011/ 2010
Number of active subscribers (K)	61,631	56,607	8.9%	59,740	3.2%	61,631	56,607	8.9%
Market share in subscribers ⁵	27.1%	25.8%	1.3 p.p.	26.5%	0.6 p.p.	27.1%	25.8%	1.3 p.p.
MOU (min.)	293	293	0.0%	289	1.4%	289	285	1.4%
ARPU (RUR.)	314	314	0.0%	321	(2.2%)	311	312	(0.3%)

The growth of MOU in the fourth quarter of 2011 versus the third quarter of 2011 was due to the seasonal increase in the volume of calls and VAS.

The quarter-on-quarter decline in ARPU was due to the decrease in roaming services and significant growth in the subscriber base.

Data traffic tripled and voice traffic increased by 10% compared to the fourth quarter of 2010.

⁵ Source – AC&M Consulting

About the Company

MegaFon OJSC – is a Russian universal telecommunications operator conducting its business in all segments of the telecommunications market. MegaFon was established in May 2002, and became the first operator with a network covering all regions of Russia. The Company and its subsidiaries have all the required licenses to operate in all of the Russian regions and the Republics of Abkhazia, South Ossetia and Tajikistan. The Company was the first in Russia to launch 3G for commercial operations and is currently no. 1 in the provision of mobile Internet services, and no. 2 as to the number of active subscribers in Russia.

Having acquired one of the leading Russian backbone operators, the Synterra group of companies, in June 2010, MegaFon entered the wireline B2B and B2G, and the wireline broadband, markets. The combined infrastructure of MegaFon and Synterra now reaches all of the Russian regions, supporting GSM 900/1800, 3G, VSAT, IP/MPLS, and NLD/ILD networks, and data and call centers, connecting to all participants in the telecommunications markets. Also, as a result of acquiring the NetByNet group, MegaFon entered the markets for wireline broad band, Internet access, digital TV and IP telephony in Moscow City and other regions.

In 2009, MegaFon became the Mobile General Partner of the XXII Winter Olympic Games and XI Paralympic Games in 2014 in Sochi.

As of January 31, 2012, the principal shareholders of MegaFon are companies of the AF Telecom Holding group, the TeliaSonera group and Altimo Telecommunications holding.

For additional information

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Schedule 1: Definitions

ARPU (Average Revenue Per User) is calculated by dividing the total revenue for the period, excluding wireline revenue and revenue from sales of handsets, accessories and other revenues, by the average number of mobile subscribers for the period and then by the number of months in the period.

MOU (Monthly Average Minutes of Use per User) is calculated by dividing total mobile minutes during the period by the average number of mobile subscribers for the period and then by the number of months in the period.

OIBDA (Operating Income Before Depreciation and Amortization) is a non-US GAAP financial measure; it should be considered as supplementary but not as an alternative to the information provided in the financial statements of the Company. OIBDA margin means OIBDA as a percentage of revenue. The Company believes that OIBDA provides a better measure of the Company's actual operational results including our ability to finance capital expenditures, acquisitions and other investments and our ability to incur and service debt. While it does not take into account depreciation of property, plant and equipment and amortization of intangible assets, which are considered as operating expenses in US GAAP, these expenses primarily represent non-cash charges related to long-lived assets acquired or constructed in prior periods. OIBDA is widely used by investors, analysts and rating agencies as a measure to evaluate and compare current and future operating performance and to determine the value of companies within the telecommunications industry. A reconciliation of OIBDA to operating income, the most directly comparable US GAAP measure, is provided in Schedule 3.

Capital Expenditures (CAPEX) comprises the cost of purchases of new equipment, new construction, acquisition of new or upgrades to software and other intangible assets, and purchases of other long-term assets, together with related costs incurred prior to the intended use of the applicable assets, all accounted for as of the earliest time of payment or delivery. Long-term assets obtained through business combinations are not included in the calculation of capital expenditures.

Free Cash Flow means cash from operating activities, less cash paid for purchases of property, plant and equipment and intangible assets, increased by proceeds from sales of property, plant and equipment. It is a non-US GAAP financial measure and should be considered as supplementary but not as an alternative to the information provided in the Company's financial statements. This metric measures the Company's ability to generate cash after accruals required to maintain and expand the Company's assets. A reconciliation of free cash flow and cash from operating activities, the most directly comparable US GAAP measure, is provided in Schedule 3.

Net positive cash position means the difference between (a) cash, cash equivalents, short-term investments and long-term deposits and (b) loans payable. It is a non-US GAAP financial measure and should be considered as supplementary but not as an alternative to the information provided in the Company's financial statements. The Company believes that this metric provides useful information as to the liquidity position of the Company after loan repayments. A description of how the metric is calculated is provided in Schedule 3 below.

Schedule 2: Consolidated Financial Statements

MegaFon

Consolidated Statements of Operations

(In millions of Rubles)

	Year ended December 31	
	2010	2011
Revenue	215,515	242,608
Cost of services	48,423	58,896
Gross margin	167,092	183,712
Sales and marketing expenses	19,471	21,841
Operating expenses	49,847	61,049
Depreciation	35,035	42,377
Amortization	3,839	5,299
Operating income	58,900	53,146
Other income/(expense):		
Interest expense	(837)	(706)
Interest income	4,008	3,591
Other gain, net	18	30
Loss on derivatives, net	(203)	(51)
Foreign currency exchange loss, net	(700)	(105)
Total other income, net	2,286	2,759
Income before income taxes and noncontrolling interests	61,186	55,905
Provision for income taxes	11,962	12,320
Net income	49,224	43,585
Less: Net income attributable to noncontrolling interests	(52)	(6)
Net income attributable to MegaFon	49,172	43,579

MegaFon
Consolidated Balance Sheets
(In millions of Rubles)

	December 31, 2010	December 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	2,667	2,887
Short-term investments	63,554	84,509
Accounts receivable, net of allowance for doubtful accounts	6,859	9,547
Accounts receivable, related parties	95	104
Inventory	3,081	4,551
Prepaid income taxes	6,975	6,957
VAT receivable	2,562	1,779
Deferred tax assets	1,166	1,972
Prepaid expenses and other current assets	7,114	7,987
Total current assets	94,073	120,293
Long-term bank deposits	305	2,002
Property, plant and equipment, net	194,872	223,718
Goodwill	7,041	15,393
Intangible assets, net	19,245	19,672
Deferred tax assets, less current portion	506	712
Deferred finance charges	665	729
Other non-current assets	760	949
Total assets	317,467	383,468

MegaFon
Consolidated Balance Sheets (continued)
(In millions of Rubles)

	December 31, 2010	December 31, 2011
Liabilities:		
Current liabilities:		
Accounts payable	6,521	9,621
Accounts payable to equipment suppliers	10,308	8,034
Accounts payable, related parties	404	465
Current portion of liability for marketing related licenses	382	402
Current portion of liability for deferred and contingent consideration	1,450	2,550
Accrued compensation and social contributions	3,028	6,187
Subscribers' prepayments	7,303	7,895
Taxes payable	1,516	2,229
VAT payable	1,294	2,965
Deferred revenue	552	954
Current portion of long-term debt	12,171	7,415
Other current liabilities	845	1,256
Total current liabilities	45,774	49,973
Debt, less current portion	20,750	36,294
Deferred tax liabilities	8,256	10,543
Asset retirement obligations	4,304	5,248
Liability for marketing related licenses, less current portion	893	621
Liability for deferred and contingent consideration, less current portion	1,731	1,829
Deferred revenue, less current portion	1,968	1,569
Other non-current liabilities	665	759
Total liabilities	84,341	106,836
Equity		
MegaFon shareholders' equity:		
Common stock (par value of 10 Rubles, 6,200,002 shares authorized, issued and outstanding)	581	581
Reserve fund	17	17
Additional paid-in capital	13,855	13,852
Retained earnings	218,371	261,950
Accumulated other comprehensive loss	(261)	(291)
Total MegaFon shareholders' equity	232,563	276,109
Noncontrolling interests	563	523
Total equity	233,126	276,632
Total liabilities and equity	317,467	383,468

MegaFon
Consolidated Statements of Cash Flows
(In millions of Rubles)

	For year ended December 31,	
	2010	2011
Cash flows from operating activities:		
Net income attributable to MegaFon	49,172	43,579
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	35,035	42,377
Amortization	3,839	5,299
Net loss on derivatives	203	51
Net foreign exchange loss	700	105
Net income attributable to noncontrolling interests	52	6
Bad debt expense	1,182	1,437
Provision for deferred income taxes	3,240	850
Amortization of deferred finance charges	180	196
Changes in assets and liabilities:		
Accounts receivable	(1,927)	(3,870)
Inventory	(1,606)	(1,414)
Prepayments and other current assets	(3,555)	(1,053)
Accounts payable and accrued expenses	448	6,962
Deferred revenue	151	3
Subscribers' prepayments	18	392
VAT, net	(519)	2,375
Net cash provided by operating activities	86,613	97,295
Cash flows from investing activities:		
Purchases of property, plant and equipment and intangible assets	(63,860)	(73,332)
Proceeds from sale of property, plant and equipment	743	449
Acquisitions of subsidiaries, net of cash acquired	(10,418)	(10,825)
Increase in short-term investments and long-term deposits	(15,275)	(18,948)
Other investing activities	(11)	—
Net cash used in investing activities	(88,821)	(102,656)
Cash flows from financing activities:		
Proceeds from long-term debt	13,728	21,486
Repayments of long-term debt	(20,105)	(14,365)
Deferred finance charges paid	(208)	(260)
Repayments of contingent consideration	—	(491)
Repayments of liability for marketing related licenses	(329)	(385)
Purchase of noncontrolling interest in consolidated subsidiaries	(100)	(40)
Dividends paid to noncontrolling interests	(147)	—
Net cash provided by/(used in) financing activities	(7,161)	5,945
Effect of exchange rate changes on cash and cash equivalents	(514)	(364)
Net increase/(decrease) in cash and cash equivalents	(9,883)	220
Cash and cash equivalents at beginning of year	12,550	2,667
Cash and cash equivalents at end of year	2,667	2,887

Schedule 3: Reconciliations of non-US GAAP financial measures (unaudited data)

OIBDA (In millions of Rubles)

	Q4 2010	Q1 2011	Q2 2011	Q3 2011	Q4 2011
Operating income	15,001	12,246	13,297	15,066	12,537
Depreciation	10,053	10,337	10,673	10,243	11,124
Amortization	1,054	1,224	1,266	1,238	1,571
OIBDA	26,108	23,807	25,236	26,547	25,232

OIBDA margin as percentage of Revenue

	Q4 2010	Q1 2011	Q2 2011	Q3 2011	Q4 2011
Operating income	25.4%	22.2%	22.7%	23.8%	19.1%
Depreciation	17.1%	18.7%	18.2%	16.1%	17.0%
Amortization	1.8%	2.2%	2.2%	2.0%	2.4%
OIBDA margin	44.3%	43.1%	43.1%	41.9%	38.5%

Positive Net Cash Position (In millions of Rubles)

	Dec31, 2010	Mar31, 2011	Jun30, 2011	Sep30, 2011	Dec31, 2011
Cash and cash equivalents	2,667	1,978	3,646	6,232	2,887
Short term financial investments	63,554	70,538	75,735	84,878	84,509
Long-term deposits	305	484	202	3,084	2,002
Loans and borrowings	(32,921)	(33,940)	(41,400)	(44,270)	(43,709)
Positive net cash position	33,605	39,060	38,183	49,924	45,689

Free Cash Flow (In millions of Rubles)

	12 months of 2010	12 months of 2011
Cash from operating activities	86,613	97,295
Purchase of property, plant and equipment and intangible assets	(63,860)	(73,332)
Proceeds from sale of property, plant and equipment	743	449
Free cash flow	23,496	24,412